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SUBJECT: CHINA/JAPAN HIGH-LEVEL ECONOMIC DIALOGUE, FORM WINS OVER
SUBSTANCE

¶1. (SBU) Summary: Form prevailed over substance at the first ever China-Japan High-Level Economic Dialogue (HLED) in Beijing December 1, 2007. The meeting was co-chaired by Chinese Vice Premier Zeng Peiyan and Japanese Foreign Minister Masahiko Koumura. Topics included macroeconomic policies, economic cooperation, environmental protection, and plans for a second HLED in 2008. After the two-hour meeting, ministers from both governments met with their counterparts, and the parties signed agreements on mutual cooperation in criminal investigations and on Japanese loans to China, including a USD 420 million loan for environmental projects. More contentious issues like China's push for recognition as a market economy and renminbi (RMB) appreciation were apparently not resolved.
"Frank" Discussions and Agreement for 2nd Dialogue

¶2. (SBU) According to Xinhua News, the talks were positive and both sides agreed to a second high-level dialogue in 2008 to be held in Tokyo. The joint communique mentioned "frank" discussions of issues concerning macro-economic policies, trade and investment, climate change, environmental protection and multilateral and regional economic cooperation. The two sides reaffirmed mutually beneficial bilateral economic ties and vowed to make a greater contribution to the sustained development of the world economy. Our Japanese Embassy counterparts informed us that President Hu will likely visit Japan next year - the first visit by a Chinese president to Japan in a decade. They also said that Prime Minister Fukuda has plans to visit China soon, possibly as early as the end of December or in early January 2008.

Zeng's Four Problems with Sino-Japan Economic Ties

¶3. (SBU) According to Chinese press reports Vice Premier Zeng identified four major problems in Sino-Japanese economic ties: a slowdown in the growth rate of bilateral trade, an unsatisfactory business environment, obstacles in technical cooperation, and fluctuating Japanese investment in China. Zeng also brought up concerns over market economy status, trade conditions, technology exports and a new emphasis on both commodities and services trade. The Vice Premier urged both sides to improve technological exchanges on energy-saving and

environmental protection and to work together to resolve global and regional economic issues.

Some Progress on Environmental Cooperation

14. (U) Japanese Embassy officials told us that the two sides made some progress on bilateral environmental protection cooperation, including a Japanese loan to China of USD 420 million loan for environmental protection projects. Both sides shared a common view on participating in the development of an effective framework for 2013 and beyond under the United Nations Convention on Climate Change, in which all major economies would agree to assume greater responsibility for environmental protection. They also agreed to enhance cooperation in recycling initiatives, improvement of water quality in the Yangtze and other major waterways, prevention of cross-border movement of waste, and sustainable forestry management.

On energy cooperation, both sides confirmed they would exchange technology and information on biomass use, clean coal, and safe coal mining practices. Japanese Embassy officials told us that environment ministers from both countries signed a statement agreeing to move forward on technology transfer and other assistance, but the statement did not include many details or concrete implementation plans.

15. (SBU) Japanese Embassy officials told us that although cooperation on environmental issues continues to grow, the Japanese often find China's approach to environmental discussions frustrating, with China repeatedly stating that it is still a developing country that lacks the technology needed to curb energy emissions. "Meanwhile, China declines to offer specific proposals to Japan indicating what kind of technology it needs. Japan is willing to provide assistance, but China needs to tell us what they need," our counterparts said.

No Agreement on Market Economy Status or Renminbi

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16. (SBU) Our Japanese counterparts told us that the Japanese side brought up RMB appreciation in the context of Japan's late 1980s "bubble economy." Sensing Chinese concerns that the Japanese yen's appreciation following the Plaza Accord led to the country's economic difficulties in the 1990s, Japan told China at the HLED that a prolonged period of excess liquidity, not the yen's appreciation, caused Japan's real estate and stock market bubble. Japanese Embassy officials informed us that in a joint statement issued following the talks, the Japanese included a sentence noting the importance of rapid RMB appreciation. (Note: The sentence read, "the Japanese side welcomed the Chinese policy for increased flexibility in the exchange rate of the RMB and expressed hope that China would make efforts toward accepting a faster pace of appreciation of the RMB's effective exchange rate." End note.) According to our Japanese Embassy contacts, the Chinese side deleted this sentence from the Chinese translation of the joint statement. (Comment: In a meeting with Econ MinCouns several weeks earlier, METI Vice Minister Toyoda confided that a major sticking point in negotiations over technology transfer for environmental and energy projects was China's poor record of IPR protection. He added that Japan hoped to leverage China's interest in these projects to make progress on IPR more broadly, noting that China had at least resumed discussing IPR with Japan after temporarily freezing bilateral cooperation in the wake of Japan's decision to participate as a third party in the U.S. WTO case. End Comment.)

17. (SBU) Regarding China's request for market economy status, Japanese embassy officials informed us that the Chinese asked Japan for a yes or no response on whether China is a market economy. The Japanese did not offer a response to the Chinese side on this issue.

Japanese Enterprises Wary of China

18. (SBU) Japanese Embassy officials told us they attribute part of the recent decline in Japanese investment in China to China's poor track record of IPR enforcement. During the HLED, the two sides agreed to broaden cooperation on IPR, including via public-private

bilateral cooperation mechanisms. "Though China has the necessary legislation in place," our contacts said, "enforcement, particularly at the local level, continues to deter investors. This is particularly true for small and medium-sized Japanese enterprises that lack the legal resources of larger companies."

¶9. (SBU) In addition to facing IPR enforcement problems, Japanese companies in China report that they are frustrated by Chinese regulations on investment and mergers and acquisitions, which they perceive as discriminatory. Political tensions resulting from former PM Koizumi's Yasukuni Shrine visits and Japanese officials' discussions with the Dalai Lama have also contributed to Japanese businesses' wariness about doing business in China, our Japanese Embassy contacts explained.

Joint Vision on Japan-China Economic Cooperation

¶10. (U) According to Japanese Embassy officials, during a February 2006 meeting, Chinese Commerce Minister Bo Xilai and former Japanese Minister of Economy, Trade, and Industry Toshihiro Nikai agreed to form a group of representatives from both governments to forge a Joint Vision on Japan-China Economic and Trade Cooperation. The group convened four times in both Japan and China over the past year and a half for discussions on the bilateral economic relationship. In conjunction with the HLED, the working group published a joint report on December 1.

¶11. (U) The report states that China has benefited from Japanese FDI, government loans, technology transfer and employment opportunities, while Japanese companies have enhanced their profits, improved their competitiveness, and increased exports to China as a result of closer bilateral economic ties. It also asserts that both countries could benefit if China shifts its development model from

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export-driven to domestic-consumption led growth. In addition, the report contains information on the difficulties facing Japanese companies in China and Chinese companies in Japan. Concerns voiced by Japanese companies include IPR enforcement difficulties, lack of transparency in the legal system, complex customs procedures and regulations, and discrimination against foreign enterprises. Chinese companies in Japan expressed concerns about their position in the Japanese market, food and product safety standards and regulations, and difficulties obtaining business visas. Both sides agreed to address these concerns through high level bilateral discussions in the future.

Nothing New This Time Around

¶12. (SBU) Our Japanese contacts told us the HLED did little to resolve controversial bilateral economic issues such as RMB appreciation, East China Sea energy exploration, or China's drive for market economy status. The meeting did, however, result in a joint statement that renewed commitments to cooperate on issues of bilateral concern such as IPR enforcement, environmental protection, and reduction of barriers to trade. Though these areas for cooperation are not new, Japanese officials expect that over the next year, terms of cooperation will become more concrete as they work toward the 2008 HLED.

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